Farm Credit Administration

Strategic Plan

Fiscal Years 1998-2003

Contents

Message from the Chairman

The need to ensure agriculture's future economic well-being and increased competitiveness of the Farm Credit System (System) dictates significant strategic change ahead for all of us as we move toward the 21st century.

With my fellow Board Members, Doyle Cook and Ann Jorgensen, we focused on this change as we planned strategically. This Strategic Plan reflects our belief that the System will continue to play an important role for agriculture and rural America in the new millenium. This plan reflects our belief that our responsibility is to provide a flexible regulatory environment that enables the System to meet rural America's changing demands for credit and other financial services within the authorities established by Congress. Our primary focus will always remain on safety and soundness, but our rules and policies will respect market forces.

This Strategic Plan is an extension of the FCA Board's vision of being the premier regulator. We all are working hard to make this vision a reality. I believe our goals and objectives provide a firm foundation for FCA's future success and the success of those we regulate.

I am proud of our employees and the Agency for having improved customer service through less burdensome rulemaking and for having enhanced communications with System institutions through our examination process. This Strategic Plan is a product of the FCA Board and staff working together and reflects an Agency serious about, and dedicated to, the job to be done.

Marsha Pyle Martin
Chairman and Chief Executive Officer
October 1, 1998

Mission

The Farm Credit Administration will promote a safe and sound, competitive Farm Credit System to finance agriculture and rural America as authorized by Congress.

LEGISLATIVE MANDATE

A healthy America requires a strong agriculture, and a strong agriculture requires a financially viable Farm Credit System (FCS or System). The Farm Credit Act of 1971, as amended (Farm Credit Act), states that Congress established the FCS because it believed that an effective credit delivery system dedicated to financing rural America would further the public interest. The FCS was established to:

- Ensure that an adequate supply of credit is available to all creditworthy producers and their cooperatives in both good times and bad.
- Provide reasonably priced credit to eligible borrowers by fostering and maintaining competitive markets in rural America.

As the independent regulator of the System, the FCA is responsible for protecting and balancing the public interest. The FCA's regulations and policies must be sound and constructive, use an approach that is proactive, manage risks within reasonable costs, and reflect the continuing changes in, and the needs of, agriculture.

FCA performs two basic functions to fulfill its mission:

- Identifying risk and taking corrective actions.
- Promulgating regulations and public policy.

Identifying Risk and Taking Corrective Action: FCA has statutory authority to examine all FCS institutions, including the Federal Agricultural Mortgage Corporation (Farmer Mac), as well as the National Consumer Cooperative Bank and the NCB Development Corporation, which are non-System entities. At October 1, 1998, the FCS was comprised of eight Farm Credit banks, 193 associations, and seven service organizations. The Agency issues written examination reports that contain an evaluation of the overall condition and performance of these institutions. The Agency's examination program is risk-based, concentrating resources on institutions having the greatest risk exposure. FCA continually identifies, evaluates, and proactively addresses risks faced by the institutions it examines.

The FCA also has authority to initiate an enforcement action against an FCS institution and its officers, directors, and employees who violate statutory or regulatory requirements or engage in unsafe or unsound practices. Enforcement actions include agreements, orders to cease and desist, civil money penalties, and orders of removal or prohibition.

Promulgating Regulations and Public Policy: The FCA has statutory authority to establish regulations and policies and interpret the Farm Credit Act and other laws applicable to the FCS. The Agency promulgates regulations and policy statements to ensure that the FCS complies with the law and operates in a safe and sound manner. The FCA is also the chartering authority for the FCS and reviews and takes action on corporate applications for mergers, consolidations, liquidation of System entities, and other corporate restructurings.

Agency personnel engage in a variety of activities that support these two basic functions. These include: long-range planning and budgeting; providing pertinent information to the Administration, Congress, the FCS, and the general public; legal counsel; economic and financial analyses; management of information and human resources and training; and administration of the performance, compensation, and benefits programs.

CONSTITUENCIES AND GUIDING PRINCIPLES

FCA's constituencies are those who have an interest in, or are potentially affected by, Agency responsibilities and activities. These include institutions regulated by the Agency, investors in System securities, the Farm Credit System Insurance Corporation, the Administration, Congress, and individual borrowers/shareholders of the FCS.

Confidence in FCA promotes confidence in the FCS. Therefore, FCA must demonstrate sound and constructive rulemaking that relates directly to its objective of controlling risk in the FCS. Through our actions, there must be no doubt that the FCA Board and management are effectively and efficiently carrying out the Agency's mission.

In the furtherance of its mission, the Agency will adhere to the following Guiding Principles:

- We will remain a fair and effective regulator that provides its constituencies with timely, accurate, and useful communications.

- We will continue to achieve a balance between costs imposed by the Agency and the benefits which accrue to our constituencies, but in no case will we compromise safety and soundness.

- We will continue to promote teamwork and a positive, productive, and family-friendly work environment.

Vision Statement and Strategic Goals and Objectives

VISION STATEMENT
FCA will be the premier regulator of financial institutions, ensuring dependable credit for agriculture and rural America.

STRATEGIC GOALS AND OBJECTIVES

The environmental assessment of internal and external factors affecting the Agency and the FCS was updated in fiscal year (FY) 1998 and the strategic goals and objectives were revised. Several meetings dedicated to refining the Strategic Plan were enhanced by customer meetings with FCS directors and chief executive officers. These System leaders were asked to identify the greatest challenges facing their institutions. These discussions added still more detail to the information provided last year when staff from key congressional committees were interviewed and asked not only to assess the environment, but also to offer ideas for strengthening FCA. Issues and trends influencing FCA's future operating environment were identified using this information. A supplemental document, "FCA's Vision 2002," provided more detail of likely internal and external trends that may have significant implications for the Agency during the next 5 years. The environmental assessment, including the underlying planning assumptions, is presented in the Appendix to this Plan.

FCA's strategic goals and objectives are:

Goal 1: Supervise risk in the Farm Credit System for the benefit of stakeholders.

Objectives

- Enhance the value and effectiveness of FCA's risk-based examination, oversight, and correction of problems in FCS institutions.
- Ensure that information systems of the FCS and FCA are effective in delivering appropriate data and analytical tools in the year 2000 and beyond.
- Enhance operations in regulated institutions through appropriate guidance.
- Ensure that FCA has the appropriate tools to address emerging risk in the FCS.

Goal 2: Maximize opportunities for the Farm Credit System to provide competitive and dependable services for agriculture and rural America.

Objectives

- Encourage new initiatives that help FCS institutions serve the evolving needs of agriculture and rural America.

- Promote better customer service at lowest cost through support of healthy competition.

- Ensure that the FCS has the ability to compete in global markets.

- Support the continuance of the FCS as a Government-sponsored enterprise (GSE) for agriculture.

Strategies to Achieve Goals and Objectives

The strategic goals reflect our focus for future action. Objectives were developed for each goal. Strategic initiatives further identify activities for the Agency during the next 5 years. Action plans for the strategic initiatives will link this Strategic Plan and shorter-term operational plans of the Agency offices. Initiatives, dynamic in nature, must be adjusted to fit a changing environment. Timely assignment of personnel, budgeting, and reporting are key ingredients of each initiative's success. The Agency's success will be captured by the performance measures delineated in the section entitled Relationship Between Strategic Goals and Objectives and the Annual Performance Goals. An overview of our approach to achieve each goal and its objectives follows.

Goal 1: Supervise risk in the Farm Credit System for the benefit of stakeholders.

FCA's examination and supervisory programs have been recognized for their high quality and effective results. This goal and its objectives focus on maintaining this high quality, as well as making still more improvements.

Areas of emphasis include the following strategic initiatives, which are designed to enable the Agency to achieve this goal and its objectives:

- Ensure that FCS institutions establish, maintain, and apply loan-underwriting standards commensurate with institutions' risk-bearing capacity and in accordance with sound lending practices.
- Implement a dynamic financial institution rating system that will identify changes in institutional risk characteristics and alert FCA to potential problems.
- Develop stress-modeling and analytical capabilities for FCA to anticipate the effects that changes in the operating environment may have on FCS institutions.
- Evaluate the adequacy and accuracy of data furnished by FCS institutions to support FCA's development of regulations and policy.
- Update and revalidate the Examiner Commissioning Program to train and develop new examiners.
- Evaluate potential risk of legislative proposals in light of safety and soundness issues.
- Communicate FCA's expectations for current events and emerging issues affecting the FCS and FCA.
- Evaluate the effectiveness of the FCS financial disclosure program.

Goal 2: Maximize opportunities for the Farm Credit System to provide competitive and dependable services for agriculture and rural America.

A major focus of the Agency's regulatory and policy development in the 1990s was the reduction of regulatory burden. In 1993, the FCA identified regulations and policies for elimination that were outdated or imposed undue burden on FCS institutions. Consistent with that effort, the FCA Board established a framework for the development of regulations with the adoption, in 1994, of its Policy Statement on Regulatory Philosophy (modified in 1995). These FCA Board actions ensure that regulations are written to implement the law, promote safety and soundness, and support the System's continued competitiveness in the marketplace, but do not impose undue burden on the System.

In addition, the Agency will focus on timely and user-friendly rulemaking and policy development processes. For example, the Agency plans to take advantage of the new technology available to make the regulatory process more interactive, efficient, and cost-effective. Near-term rulemaking projects include investments, borrower rights, and termination regulations for banks and large associations. The FCA Board recently approved the solicitation of comments from the public on regulations that may be outdated, ineffective, or duplicative of other requirements. Based on the comments received, the FCA Board will propose rulemaking or policy initiatives to address these concerns.

Several of the more important initiatives that will be undertaken to satisfy the objectives supporting this goal are to:

- Promote the FCS's delivery of services to young, beginning, small, and minority producers.

- Promote strategic alliances among FCS institutions and with third parties in order to benefit eligible borrowers.

- Enhance FCA's intra-Governmental coordination on issues of significance to the FCS.

- Ensure that regulatory activities do not pose roadblocks to international agricultural commerce.

- Establish conditions governing bank or association termination and continued service to the designated territory.

RESOURCE NEEDS

FCA's direct obligations budget for FY 1998 was $34.4 million, down $1.5 million from FY 1997. The FCA is revising its financial management system to account for costs by goals in FY 1999. Since more than 80 percent of total costs are salaries and benefits, staff costs supporting each goal are the primary costs of obtaining the desired outcomes.

Since FY 1995, actual costs have declined primarily because of reductions in personnel. Staff levels have declined 43 percent from their peak in FY 1988. The budget for FY 1999 projects a 4 percent increase. The human resource forecast is for relatively stable staff numbers over the Strategic Plan period, but new skills and a redirection of efforts will be required to achieve the goals and objectives in this Plan. Expected increases in the cost of labor will be partially offset by investments in technology and by reengineering processes to produce better results at less cost. The strategic goals and objectives reflect our commitment that FCA will continue to be a cost-effective regulator. The Agency is exploring options to use our resources and systems at higher efficiency to permit reimbursable activities. So long as the FCS remains healthy, FCA's resource needs should not increase significantly over the planning horizon.

In 1995, the Agency conducted a long-range staffing study. This strategic effort positioned the Agency to move into the next century. Efforts continue to refine this study, improve productivity, align staff with strategic needs, and develop the critical skills to accomplish the FCA's mission, strategic goals, and objectives. Since implementation of the Five-Year Staffing and Structure Plan (Staffing Plan) in April 1996, 72 staff positions and two management layers have been eliminated. In FY 1997, the number of field offices located outside headquarters was reduced to 4, down from 11 in 1991.

The cost to the users of the FCS, when measured in terms of FCA's expenditures compared to the System's average earning assets, has been reduced substantially. Since FY 1992, the peak cost year, FCA's cost has been reduced by approximately one-third, from 6.4 basis points to a projected 4.4 basis points for FY 1998.

Relationship Between Strategic Goals and Objectives and the Annual Performance Goals

The Strategic Plan was refined in FY 1998 by the FCA Board working with the Leadership Team. Two goals were revised to reflect the mission of the FCA serving its public in a rapidly changing environment for agriculture and the financial services industry. The third goal, which focused on internal efficiency and effectiveness, has been recast as Management Focus Areas in the Strategic Plan (Appendix A-8). The results achieved by the Agency through the Goals, Objectives, and Initiatives identified in the Strategic Plan will be reported through an integrated performance measurement system. This system is predicated on four desired outcomes, or results, for the Agency's operations which are closely linked to the Agency's strategic goals. Agency-level performance measures have been developed for each outcome. The performance measures identified below will be influenced by the initiatives associated with each goal. Many measures are also indirectly linked to initiatives in the goals and will be influenced by this relationship as well. For instance, a regulation or policy-related initiative in Goal 2 will often relate to the safety and soundness of the FCS, which would affect measures listed under Goal 1.

In addition to the Agency-level measures, each FCA operating unit has developed performance measures for its functional responsibilities. These measures are linked to the Agency-level measures and will be included in staff's individual performance standards as appropriate. By linking the Agency's goals to performance measures and then linking those measures to staff performance standards, every employee in the Agency is working toward achieving FCA's goals and objectives.

The Agency's performance measures are a "balanced" set of measures. That is, while achieving the desired outcome or goal is important, consideration must be given to the cost (inputs) and the accuracy and integrity of the products (outputs such as examination reports, regulations, etc.) used to achieve the outcome. Otherwise, the desired result may be obtained, but in a cost-prohibitive, or possibly inappropriate, manner. A balanced group of measures allows management to assess the totality of the Agency's operations and provides the needed information from which future strategic decisions will be made. Development of performance measures was accomplished with input from the FCA Board Members, the Leadership Team, and all Agency offices.

FCA will include the measures, along with the accompanying performance goals, in its revised FY 1999 Annual Performance Plan. That plan will be submitted to the Office of Management and Budget (OMB) along with the FY 2000 budget request. The following list depicts the linkage between the Agency's goals and outcomes, and highlights the measures developed to monitor FCA's performance.

Goal 1: Supervise risk in the Farm Credit System for the benefit of stakeholders.

Desired Outcome: Effective Risk Identification and Corrective Action

Performance Measures to Be Employed:

1. The health of the FCS, as depicted by the percentage of FCS institution assets assigned to each of the composite numeric FIRS ratings, i.e., 1 through 5, with 5 representing the poorest rating (FIRS stands for Financial Institution Rating System, which is a system for rating institutions on their capital, assets, management, earnings, liquidity, and sensitivity to market risk).

2. The number of direct-lender institutions with adversely classified assets to risk funds less than 100 percent divided by the total number of direct-lender institutions.

3. The total assets of direct-lender institutions with adversely classified assets to risk funds less than 100 percent divided by the total assets of direct-lender institutions.

4. The total assets of direct-lender institutions complying with all minimum capital ratios (permanent capital ratio, total surplus ratio, core surplus ratio, net collateral ratio) divided by the total assets of direct-lender institutions.

5. The 3-year average return on average assets of FCS institutions.

6. The percentage of FCA examinations of FCS institutions meeting statutory examination frequency requirements.

7. Customer acceptance of FCA's examination and supervisory programs through the average of the ratings received on the following survey questions (1 to 5, with 1 being the highest):

   - The board and management believe the findings of the examination will assist (or have assisted) the institution in correcting identified weaknesses.

   - The board and management believe the actions required by the enforcement document will assist (or have assisted) the institution in correcting identified weaknesses.

8. The number of direct-lender institutions with adversely classified assets to risk funds greater than 100 percent with corrective action plans that mitigate the excessive risk.

9. The percentage of FCS institutions and FCA that develop programs to meet established time lines to achieve year 2000 compliance in all mission-critical systems by 12/31/99.

10. The percentage of FCS institutions and FCA having contingency plans in place when mission-critical systems have not been certified to be year 2000 compliant by 12/31/98.

Goal 2: Maximize opportunities for the Farm Credit System to provide competitive and dependable services for agriculture and rural America.

Desired Outcome: Effective Regulation and Public Policy

Performance Measures to Be Employed:

1. The percentage of regulatory projects completed compared with projects included in the Board-approved annual Regulatory Performance Plan.

2. The percentage of regulations completed that utilized "special" customer service focus or features.[1]

3. The percentage of regulations that customers believe meet the regulations' original objectives.

In addition to these two goals, the FCA Board and Leadership Team have determined that two other outcomes relating to the Agency's administrative operations and external relationships should also be measured to accurately assess the effectiveness and efficiency of the Agency. To that end, we include below these desired outcomes and their performance measures. As with the measures for the two strategic goals, these measures will also be carefully monitored.

Desired Outcome: Effective and Efficient Agency Administration

Performance Measures to Be Employed:

1. An unqualified opinion received on FCA's financial statements.

2. The number of material weaknesses noted in the Federal Managers' Financial Integrity Act letter from the Agency Chairman/CEO to the President.

3. The cost of FCA to FCS borrowers (FCA's actual expenses divided by average total System assets expressed as basis points).

1. Special customer service focus or features include "fast-track," interim, and "direct" final rules, Advance Notice of Proposed Rulemaking actions, meetings with or use of customer "focus groups" prior to proposing new rules, town meetings, hearings, negotiated rulemakings (Reg-Neg), etc.

Desired Outcome: Effective External Relationships

Performance Measures to Be Employed:

1. The percentage of inquiries and complaints from Congress and the general public that:

   • Are answered within a specified time frame, and

   • Do not require supplemental responses due to inaccurate or incomplete information.

2. Congressional rejection of final FCA regulations and proposed legislative initiatives, or requests for delay in FCA Board action on regulations.

3. The percentage of the Agency's annual budget request approved by Congress without conditions.

4. The percentage of external reports issued on time, as specified in the Publication Schedule.

Key External Factors Affecting Strategic Goal Achievement

Planning is partially based on a limited base of knowledge about key factors that can determine success or failure. Therefore, business strategies rely, in part, on predictions and probabilities. Success is a function of controlling those factors that are within an organization's power and wisely managing around those that are not.

In developing this Strategic Plan, FCA identified several external factors that could significantly affect achievement of strategic goals. These factors are categorized into two areas—legislative and economic.

Legislative

- Financial Modernization — Proposals to repeal the Glass-Steagall Act, which for more than 60 years has separated banking from commerce, combined with other reform measures, would consolidate the financial services industry and reduce the number of niche service providers. Without counterbalancing measures for the FCS to maintain a level playing field, its viability and, thus, its safety and soundness could be threatened.

- Change in the bank regulatory structure is expected to move from prohibited activities to risk-management requirements to protect the public interest.

- New Funding Sources — Commercial banks' greater access to funding through the Federal Home Loan Bank System and Farmer Mac, as new sources of long-term funds, could diminish the competitive position of the FCS.

- Eliminating GSE status for the FCS — Within the context of financial reform, a move to eliminate the System's GSE status without significant reform measures for the System and other GSEs, while extending new powers to commercial banks, could seriously erode the System's competitive position in rural credit markets and increase the cost to farmers and ranchers who need competitive alternatives.

- The focus on year 2000 will require a change in priorities and an increase in reporting and testing to ensure that mission-critical systems of the FCA and the FCS institutions are year 2000 compliant.

- The U.S. Department of Agriculture report on credit availability to young, beginning, small, and minority producers, entitled "National Commission on Small Farms," will cause review and, possibly, new legislative efforts to improve opportunities for underserved sectors of agriculture, which will have both operational and public policy impacts on the FCS.

Economic

- Globalization Trends — Traditional boundaries for the world's commodity and financial markets are disappearing rapidly due to technological breakthroughs in the communication and production areas, as well as new and enhanced trade agreements. The new market environment for U.S. producers will be characterized by greater price and income volatility and likely changes in the comparative advantage for some commodities. These developments portend greater risk for agricultural producers and lenders.

- Agriculture — Accelerating consolidation, use of biotechnology, and the vertical integration of agribusinesses are reshaping rural America, along with the financial and infrastructure needs in the marketplace, at a revolutionary pace.

- Fiscal and Monetary Policy — Large swings in Federal spending for farm support programs—or their elimination—coupled with significant changes in the money supply can affect income levels and interest rates, leading to financial hardships for farmers and lenders.

- Recession — A major economic recession, especially one that is worldwide, would be very damaging to agriculture, as falling demand decreases price and income levels. Trouble for agriculture may again demonstrate the importance of the FCS as the only lender willing, and with a mandate, to finance creditworthy agricultural producers through good times and bad.

- Natural Forces — Because weather is uncontrollable, world agricultural production levels are subject to wide swings, leading to occasional gluts and shortages, with closely associated valleys and peaks in prices. Boom-and-bust economics can be a precursor for land price surges. Thus, the health of agriculture and the FCS is inextricably connected to the environment and the earth's natural resources.

Program Evaluations

Information gathering is an important part of the planning process. In gathering the information necessary to develop FCA's Strategic Plan, we relied on numerous sources of information, both internal and external. These sources included staff studies on systemic risk issues, outreach programs with System institutions, and Government reports on the agricultural economy. Agency performance measures are supported by performance and cost data produced by several office-specific systems. These systems will be refined and more will be developed as needs are identified in this initial year of implementing performance measures.

Three types of audits are the primary sources of evaluative information used to assess performance under the Strategic Plan: Agency self-assessments, audits by the Agency's Inspector General, and audits by external parties, such as the General Accounting Office or the Agency's external auditor. OMB guidance is used to periodically review and report on the Agency's systems for internal controls, financial management, information resources management, and budgeting control. Corrective actions designed to overcome problems identified by these audits may be integrated into the strategic planning process, as appropriate.

The FCA Inspector General routinely evaluates significant programs within the Agency and makes recommendations for improvements. The Agency's audit follow-up program ensures that timely decisions are made relative to these recommendations and that corrective actions are taken as needed. The Inspector General is a member of the Leadership Team and uses that forum to keep program evaluation issues before Agency management. Further, the Inspector General's Semiannual Reports to the Congress (March 31 and September 30) provide a vehicle to communicate any issue, disagreement, or other problem identified by program evaluations. The Inspector General's recommendations have influenced numerous improvements in Agency operations. Recently completed and planned program evaluations by the Inspector General include:

- Year 2000 — This evaluation will assess FCA's preparation for transitioning the Agency's internal computer systems to the new millennium and testing the compliance of existing systems.

- Development of performance measures by Agency offices — This evaluation will focus on whether measures have been developed for all significant internal functions, whether standards have been developed for measurements, and whether reliable information systems exist to support application of those metrics.

- Effectiveness of FCA's enforcement activities.

- Effectiveness of FCA's rulemaking processes.

- Effectiveness of the Agency's small purchases program.

- Effectiveness of FCA's development of subject matter specialists.

Finally, the Agency has an extensive set of internal controls by which it monitors its operations. Findings from all of these operational assessments are considered in the development of the Strategic Plan.

FCA Board and Leadership Team Concurrence

FCA management and policy making is vested in a three-member board. Members of the Leadership Team are charged by the CEO to carry out the Board's mandate and implement programs as provided for in the Farm Credit Act and this Strategic Plan.

The FCA Board and Leadership Team are committed to working with our employees and with our constituents to make this an effective Strategic Plan.

The FCA Board:

Marsha Pyle Martin
Chairman and Chief Executive Officer

Doyle L. Cook, Member

Ann Jorgensen, Member

The Leadership Team:

Donald P. Clark, Director
Office of Resources Management

Thomas G. McKenzie, Director
Office of Policy and Analysis

Eileen M. McMahon, Director
Office of Congressional and Public Affairs

Jean Noonan, General Counsel
Office of General Counsel

Roland E. Smith, Chief Examiner
Office of Examination

Eldon W. Stoehr, Inspector General
Office of Inspector General

Appendix

ENVIRONMENTAL ASSESSMENT

The most significant environmental trends affecting FCA's mission are discussed below. These trends and the assumptions that follow were the foundation for formulating the goals and objectives in this Strategic Plan.

Financial Industry and Marketplace

During the planning period, agricultural lenders will face a changed lending environment and a new set of risks. Some risks will emerge because of the increased reliance of farm income on world market conditions and greater volatility in commodity prices as a result of the Federal Agriculture Improvement and Reform Act of 1996 (1996 Farm Act) and resulting planting adjustments. Other risks will arise from increasingly aggressive competition among traditional and nontraditional lenders for good loans. The condition of financial institutions lending in the agricultural arena may undergo significant change as the dynamics of agricultural economics and production advances cause shifts in the profitability of various agricultural sectors.

Historic changes in U.S. farm policy in 1996 will continue to cause a gradual increase in the dependence of agricultural income on world market conditions. Export of agricultural products is vital to the economic well-being of the U.S. farm sector and, accordingly, surpluses and shortages in world commodity supplies will significantly affect the profitability of farmers and ranchers and their cooperatives. The value of farm exports is volatile and subject to forces that are both diverse and unpredictable. These forces include U.S. foreign policy, monetary policy, trade policy, national and international economic conditions, and weather. Risk is increased when growth in mortgage lending on farmland purchases is fueled by factors other than the income-generating capacity of real estate, such as speculative purchases of real estate or unsustainably high commodity prices. Risk in operating credits can also change significantly from initial estimates as changes occur in national and international supplies, interest rates, or as countries announce their trade needs.

The agricultural customer base for financial institutions is shrinking in number and changing rapidly in size of operation. The number of small, part-time farmers will continue to increase, but they will be less dependent on farming for their livelihood. The trend toward fewer but larger farms will continue, and the demand by lenders to serve this profitable market niche will become increasingly competitive. This competitive market may fuel a trend toward pricing loans to retain market share of this segment rather than pricing for risk inherent in loans. The demographics of farmers and ranchers will also cause changes in the lending programs of FCS institutions. The trend for moderate and small size farmers and ranchers to seek off-farm employment to supplement agricultural income will continue. As their funding needs change, additional pressure will be placed on FCS institutions to change to meet their requirements.

Farm Credit System

Tax law interpretations, new technology, competitive forces, and other developments in the financial services industry will prompt additional mergers and consolidations in the FCS. In 1983, there were 932 FCS institutions, but by October 1, 1998, that number had declined over 78 percent to 201. Although consolidations and mergers are expected to continue and will result in fewer FCS institutions at both the wholesale and retail levels, the workload for FCA will not decrease proportionately over the planning period because larger, more complex institutions will likely require closer supervision. System consolidation is a key issue for FCA, as risk becomes concentrated into fewer, larger, and more complex institutions at the bank and association level. Risk identification and risk management programs are key to successfully managing these changes.

Most FCS institutions will continue to operate as single purpose lenders with significant concentrations in few industries. Because of the limitations of their charters, and without selling off portions of the loan portfolios or participating in other industry loans, they will continue to struggle to diversify their portfolios to escape the risks in their industry concentrations. To mitigate concentration risk, they will need to find innovative ways to continue to safely lend to agricultural producers, processors, and marketers. Such new programs will change the operations of FCS institutions and open new opportunities and challenges. FCA must continue to be at the forefront of these changes and ensure that it develops the expertise to examine complex programs as they evolve.

Technological Changes

Two customer groups are emerging—those who want services delivered through a personal computer (high tech) and those who demand a relationship with a banker who knows them personally (high touch). The increased demand for electronic banking through the use of worldwide communication networks and sophisticated data management capabilities will make possible a whole new array of services and products from financial vendors. This technology will enable lenders to steadily increase the business handled over communication lines, thereby changing the way they conduct business. Similar technology will enable FCA to regulate the FCS with less paper flow and more off-site examinations. Opportunities also exist to use technology to electronically transmit data and/or communicate between System institutions and the FCA.

FCA will need to continue to address the risk issues associated with the year 2000 date change, both internally and with the FCS. FCA has a plan in place to correct the date change for FCA mission-critical and other significant information systems prior to the year 2000. The FCS is dealing with the problem; however, many other forward-looking organizations that recognized the problem earlier have found that the year 2000 problem is more massive and costly than predicted. The early recognition of the problem by the System offers reasonable assurance that corrective actions will be implemented.

Major breakthroughs in genetic research and new production methods will not only affect the varieties of agricultural products grown but where and how they are produced. Biochemical engineering, modern cultivation practices, and environmental concerns will contribute to new developments in production capacity and economics. These developments will alter the risk characteristics of some lending programs and may change the risk profile of System institutions and pose new challenges for FCA examiners.

Legislative and Regulatory Initiatives

The 1996 Farm Act introduced an entirely new price and income support structure for agriculture by offering fixed payments to producers for 7 years, regardless of current market prices. This legislation eliminated all deficiency payments and set-aside acreage requirements, giving producers the flexibility to grow whatever they want with few restrictions. The result of this is potential additional risk to those institutions for which FCA has oversight responsibility. FCA must continue its vigilance in monitoring risk and assessing risk management in the FCS.

Changes in the agricultural economy, the financial industry, and FCS structure will continue to drive FCA's regulatory and policy-making agenda during the planning period. In addition to safety and soundness, emphasis will continue to be placed on client and customer satisfaction, reducing regulatory burden, and the increased use of electronic communications technology to encourage public participation in the rulemaking process. The FCA Board will promote innovative approaches to emphasize rules that are user-friendly and explain complex issues in layman's terms. Emphasis will also be placed on developing comprehensive educational tools after the adoption of significant regulations. These materials will include key topic summaries for Congress, congressional staff members, and other audiences.

Budget and Staffing Issues

FCA will continue to consider cost containment measures and respond to the Government's streamlining initiatives under the National Performance Review (NPR). In 1996, FCA implemented the Staffing Plan, which is responsive to the NPR report Creating a Government that Works Better and Costs Less. The Staffing Plan contained many recommended changes that since implemented have enabled the Agency to function more efficiently. Several offices were restructured, and 72 positions and two management layers have been eliminated. The Agency will continue to be challenged to align available staff resources to emerging skills requirements.

FCA, however, must always be able to carry out its financial and regulatory responsibilities. A deep economic recession, a major financial crisis, or widespread distress in the agricultural sector could place an acute burden on the Agency's available resources. Therefore, FCA must remain alert to any threat to its ability to carry out its mission and be prepared to adjust resources as the need arises.

Improving Agency productivity by maintaining and enhancing employee satisfaction is a priority. FCA will utilize its talent base to the maximum advantage. Cross-training, rotational assignments, and new applications of information and communication technology will allow the Agency to address changes in the FCS in a timely and effective manner.

PLANNING ASSUMPTIONS

FCA used the information in the environmental assessment to conduct an analysis of the Agency's internal strengths and weaknesses, as well as external opportunities and threats. This analysis formed the foundation for the planning assumptions listed below. It also helped define the Agency's goals for the future.

External Assumptions

Legislative and Regulatory Changes

- The FCS will explore expanded authorities to create new business opportunities.

- Competitors will resist any perceived expanded authorities by the System.

- The role of GSEs will continue to be evaluated by Congress and the Administration.

- There will be a need for clear and persuasive explanations of FCA's regulatory and policy actions and rationales, and ongoing communication with the FCS, Congress, and the public.

- Commercial banks will seek greater access to GSE funding—a proposal that would pose new risks, management challenges, opportunities for the FCS, and regulatory demands on FCA.

- There will be continued pressure on the System to advance social purpose programs.

- Expansion of the Federal Home Loan Bank charter will intensify competition for the System, presenting challenges to the System.

- The direction and future of the Farm Services Agency will continue to be debated, raising the possibility of FCS and FCA involvement.

Financial and Agricultural Industries

- Overall net farm income, after adjustments for inflation, will stay at a relatively flat level during the planning period, but with significant shifts in profitability among commodity types and geographic areas due to the 1996 Farm Act.

- The riskier environment brought about by a reduced Government role will lead to greater year-to-year price and income volatility, making debt repayment capacity more uncertain. This environment will lead to increased use of risk-management tools, some of which will be new and will require both farmers and lenders to acquire new skills.

- Trade barriers and reduced growth in foreign markets will challenge globalization of, and limit new and expanded markets for, American agriculture.

- Economic uncertainties in Pacific Rim countries pose increased risk, challenges, and opportunities for American agriculture.

- Portfolio concentrations in the FCS that are sensitive to export market or foreign currency fluctuations contain inherent risk exposure.

- The agricultural industry will see moderate growth in loan demand, reduced repayment capacity margins, and gains in real farmland values (i.e., adjusted for inflation).

- Interest rates will be marked more by short-term volatility than by significant upward or downward trends.

- The traditional customer base of the FCS, the mid-sized family farm, will continue to migrate toward a bimodal distribution of large agribusinesses and small part-time operators, significantly changing the way the System conducts its business.

- Increasing use of new and complex financial instruments will continue to present challenges and risks.

Farm Credit System

Structure

- Merger and consolidation activity in the FCS will concentrate risk in fewer and larger institutions.

- Associations will become more independent of Farm Credit banks, pursue strategic alliances with each other, and increasingly become the focal point for risk in the FCS.

- Farm Credit banks will focus on wholesale lending and forming strategic alliances with non-System organizations to provide new financial services to customers.

Competition

- FCS institutions will face intense competitive pressures from both traditional and nontraditional agricultural lenders, resulting in innovative System responses and corresponding regulatory challenges.

- New lending initiatives and related service programs, combined with increasing emphasis on growth, will magnify intra-System competition.

Market Share

- The FCS's balanced marketing efforts will be crucial to its long-term success. During a stable agricultural economy, competition for good loans will increase significantly for the FCS. Maintaining market share will be difficult.

- Consolidation in the commercial banking industry will continue, and large national banks may become more competitive in the agricultural arena.

- Small community banks lacking operating efficiencies will find it increasingly difficult to compete with large banks and consolidated FCS institutions.

- Desire for growth and market share within the FCS may cause it to relax lending standards and use inappropriate loan-pricing practices.

Public Information

- An effective, well-rounded education and information program will enhance public and constituent understanding of FCA's role and value as an independent regulator.

- FCA will continue to provide accurate information about System authorities and Agency actions.

Technological Changes

- Technology will continue to develop at a fast pace with significant advancements in hardware, software, and telecommunication capabilities.

- Secure electronic commerce on the Internet will change the way financial products and services are delivered and money is exchanged.

- Year 2000 compliance will require significant remedial expenses or mergers for some institutions.

- The FCS will aggressively pursue technology-based, streamlined lending practices, many of which will challenge existing business lending practices and require regulatory adjustments.

INTERNAL ASSUMPTIONS

Regulatory and Examination Issues

- The Agency will continue its commitment to effective regulations and policies.

- The Agency will continue to emphasize ongoing, risk-based examinations and updated practices to ensure timely identification of risks and efficient use of resources.

- The dynamic FIRS and quarterly adjustments to FIRS ratings will enhance the Agency's ability to measure and supervise risk in System institutions.

- FIRS guidelines provided to System institutions will enhance understanding of performance expectations for FIRS ratings.

- The Agency will continue to emphasize reliable, meaningful disclosure as a means of increasing the accountability of management and boards of directors to stockholders, and to ensure that investors are provided the necessary information to keep appropriately informed.

Management Systems and Operations

- Reliable financial management records and information systems will provide an opportunity for improving management decision making.

- Reengineering of Agency processes will continue to increase efficiency and effectiveness.

- Meaningful performance measures will improve Agency results and allow accurate and appropriate evaluation of the FCA's performance under the Strategic Plan.

- The effectiveness of the Agency will improve as all employees are involved and better understand their roles in implementing the Strategic Plan.

- The Agency will pursue alliances with other regulators to enhance efficiency, increase revenue, and reduce operating costs.

- Public scrutiny of the Agency's budget will continue.

Technological Changes

- The Agency's client/server computer network environment will continue to provide opportunities for increased efficiency and effectiveness; costs and security risks will be continuing challenges.

- New technology will provide an opportunity for alternative work environments and cultures.

- Enhanced computer skills will allow improved use of new technology.

- Technological capabilities will be updated to meet business needs.

- Electronic access to FCS information will enhance the examination process.

- FCA will meet its year 2000 readiness plan.

Human Resources Management

- FCA staff will continue to be skilled, experienced, talented, and highly regarded.
- Staff skills will need to keep pace with emerging issues and changing priorities.
- Contingency planning will position FCA to respond to changing conditions.
- A competitive compensation level will enable FCA to attract and retain high quality employees.
- Striking a balance between the Agency's commitment to a family-friendly workplace and Agency needs will present challenges and opportunities.
- Employees who are committed to making FCA the premier regulator will continue to be rewarded.
- Recommendations from employee task forces and resulting decisions will be vital to ongoing management planning.

MANAGEMENT FOCUS AREAS

The costs of the FCA are assessed to the FCS institutions under the Farm Credit Act. FCA must provide effective and efficient regulation of the FCS for the benefit of agricultural producers and others designated in the Farm Credit Act while protecting the investing public from unreasonable risks in FCS securities. The strong correlation between sound, effective regulation and the risk-adjusted price of FCS securities ensures competitive interest rates for agriculture from this GSE source. The cost of regulation is a cost of doing business for the FCS, and the FCA Board controls the operating costs of FCA through business planning and formal budgets that are the basis for the assessments. Management will ensure that FCA meets its mission and that the continuing benefits of regulation are maintained by operating FCA as a business, weighing the costs of its actions against the long-term benefits. Management will consider innovation in practices, franchising services, outsourcing and investment in technology to acquire the skills and services necessary at the best value for FCA.

Human Resources

FCA must hire, train, motivate, and reward employees appropriately to successfully meet its mission in a cost-effective manner. FCA is committed to maintaining a 5-year human resources plan. The plan will address numbers of employees, grades, training, and Equal Employment Opportunity and skills objectives needed for essential operations and to implement the Strategic Plan. Compensation, benefits, performance measurement, and rewards will be structured to ensure premier performance by FCA.

Financial Plans

The Chief Financial Officer will develop a 5-year financial plan to identify resource needs and analyze the impact on costs, assessments, and effectiveness. This plan will consider strategic initiatives, the orderly replacement and upgrades of equipment and systems, and programs required for FCA operations. FCA will analyze the net changes in resources required over the plan period, as well as develop contingencies for changes in the operating environment. The financial plan will provide the FCA Board a resource for approving budgets and approving the Strategic Plan.

Information Technology Plans

The role of IRM in the operations of FCA is to deliver timely and cost-effective information management services and systems that significantly contribute to the accomplishment of FCA's mission. The following three major responsibilities contribute to fulfilling this role:

> Policy and Planning includes IRM policy, planning, reviews, quality assurance, and security.
>
> Information Management includes records management, library operations, and information collection.
>
> Technology Management includes technology assessment, acquisition management, system and network operations, "helpline" services, loaning of equipment, systems development, database administration, technical training development and delivery, and security implementation.

The Agency will continue to promote the use of technology to help accomplish the FCA mission more efficiently and effectively. Agency technology investments will be evaluated and chosen through a disciplined process that weighs the risks against expected returns or results. Cost containment will remain a high priority, and the most cost-effective means of conducting business will be pursued.

The establishment of information oversight committees and a formal IRM planning process has been instrumental in permitting the FCA to implement an efficient and effective IRM program. The FCA's Leadership Team provides executive direction and oversight to the Agency's operations, including the IRM program. The IRM Operations Committee (IRMOC) provides business unit input to the Leadership Team as part of its role in recommending a 5-year IRM plan. The IRMOC also coordinates operational matters and provides a forum for communication between the Director of the Information Resources Division (IRD), IRD staff, and the other IRMOC members.

Communication with the Public

The FCA recognizes the importance of communicating information and receiving feedback from its customers to improve service and accomplish its mission. Programs such as the periodic meetings with FCS institutions, Internet access, and publications and reports will be reviewed

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